

Vera Bradley, Inc.
Form 10-K
April 03, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the Fiscal Year Ended February 2, 2013

OR

.. **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the Transition Period From to

Commission File Number: 001-34918

VERA BRADLEY, INC.

(Exact name of registrant as specified in its charter)

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| | |
|--|--|
| Indiana (State or other jurisdiction of incorporation or organization) | 27-2935063 (I.R.S. Employer Identification No.) |
| 2208 Production Road, Fort Wayne, Indiana (Address of principal executive offices) | 46808 (Zip Code) |
| (877) 708-8372 (Registrant's telephone number, including area code) | |

Securities registered pursuant to Section 12(b) of the Act:

| | |
|----------------------------|--|
| Title of each class | Name of each exchange on which registered |
| Common Stock | The NASDAQ Global Select Market |

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

The aggregate market value of the registrant's voting common stock held by non-affiliates of the registrant as of July 28, 2012 was \$441,178,250.

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The registrant had 40,602,546 shares of its common stock outstanding as of April 2, 2013.

DOCUMENT INCORPORATED BY REFERENCE:

Portions of the registrant's definitive proxy statement for the 2013 Annual Meeting of Shareholders are incorporated by reference into Part III of this Annual Report on Form 10-K.

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Forward-Looking Statements

This annual report contains forward-looking statements that are subject to risks and uncertainties. All statements other than statements of historical or current fact included in this report are forward-looking statements. Forward-looking statements refer to our current expectations and projections relating to our financial condition, results of operations, plans, objectives, strategies, future performance, and business. You can identify forward-looking statements by the fact that they do not relate strictly to historical or current facts. These statements may include words such as anticipate, estimate, expect, project, plan, intend, believe, may, might, will, should, can have, and likely and similar meaning in connection with any discussion of the timing or nature of future operating or financial performance or other events. For example, all statements we make relating to our estimated and projected earnings, revenues, costs, expenditures, cash flows, growth rates, and financial results, our plans and objectives for future operations, growth, initiatives, or strategies, or the expected outcome or impact of pending or threatened litigation are forward-looking statements. All forward-looking statements are subject to risks and uncertainties that may cause actual results to differ materially from those that we expected, including:

possible adverse changes in general economic conditions and their impact on consumer confidence and consumer spending;

possible inability to predict and respond in a timely manner to changes in consumer demand;

possible loss of key management or design associates or inability to attract and retain the talent required for our business;

possible inability to maintain and enhance our brand;

possible inability to successfully implement our growth strategies or manage our growing business;

possible inability to successfully open and operate new stores as planned; and

possible inability to sustain levels of comparable-store sales.

We derive many of our forward-looking statements from our operating plans and forecasts, which are based upon detailed assumptions. While we believe that our assumptions are reasonable, we caution that it is difficult to predict the impact of known factors, and it is impossible for us to anticipate all factors that could affect our actual results.

For a discussion of these risks and other risks and uncertainties that could cause actual results to differ materially from those contained in our forward-looking statements, please refer to **Risk Factors** in Item 1A of this report.

We caution you that the risks and uncertainties identified by us may not be all of the factors that are important to you. Furthermore, the forward-looking statements included in this report are made only as of the date hereof. We undertake no obligation to publicly update or revise any forward-looking statement as a result of new information, future events, or otherwise, except as required by law.

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PART I

Item 1. Business
Our Company

Vera Bradley is a leading designer, producer, marketer, and retailer of stylish and highly functional accessories for women. Our products include a wide offering of handbags, accessories, and travel and leisure items. Over our 30-year history, Vera Bradley has become a true lifestyle brand that appeals to a broad range of consumers. Our brand vision is accessible luxury that inspires a casual, fun, and family-oriented lifestyle. Our brand positioning emphasizes the high quality, distinctive and vibrant styling, and functional design of our products. Frequent releases of new designs help keep the brand fresh and our customers continually engaged.

We generate net revenues by selling products through two reportable segments: Direct and Indirect. As of February 2, 2013, our Direct segment consisted of sales of Vera Bradley products through our 65 full-price and 11 outlet stores in the United States; 15 department store locations in Japan; our websites, verabradley.com and verabradley.co.jp; and our annual outlet sale in Fort Wayne, Indiana. As of February 2, 2013, our Indirect segment consisted of sales of Vera Bradley products to approximately 3,400 specialty retailers, substantially all of which are located in the United States, as well as select department stores and third party e-commerce sites. For financial information about our reportable segments, refer to Note 14 of the Notes to Consolidated Financial Statements set forth in Part II, Item 8. Financial Statements and Supplementary Data, of this report.

The Company utilizes a 52-53 week fiscal year end. Effective January 1, 2008, we changed our fiscal year to end on the Saturday closest to January 31. As such, fiscal year 2013 ended on February 2, 2013 and reflected a 53-week period; fiscal years 2012 and 2011 ended on January 28, 2012, and January 29, 2011, respectively, and reflected 52-week periods.

Reorganization Transaction and Stock Split

Vera Bradley, Inc. was formed as an Indiana corporation on June 23, 2010, for the purpose of reorganizing the corporate structure of Vera Bradley Designs, Inc., which was incorporated in Indiana on November 15, 1982. On October 3, 2010, the shareholders of Vera Bradley Designs, Inc. contributed all of their shares of Class A Voting Common Stock and Class B Non-Voting Common Stock of Vera Bradley Designs, Inc. to Vera Bradley, Inc. in return for shares of Vera Bradley, Inc. Class A Voting Common Stock and Class B Non-Voting Common Stock on a one-for-one basis. In addition, effective October 3, 2010, Vera Bradley Designs, Inc. converted from an S Corporation to a C Corporation for income-tax purposes. Further, on October 18, 2010, Vera Bradley, Inc. recapitalized all of its Class A Voting Common Stock and Class B Non-Voting Common Stock into a single class of common stock and effectuated a 35.437-for-1 stock split of all outstanding shares of its common stock. These events collectively are referred to as the Reorganization. As a result of the Reorganization, Vera Bradley Designs, Inc. became a wholly owned subsidiary of Vera Bradley, Inc.

The only significant asset of Vera Bradley, Inc. is its investment in Vera Bradley Designs, Inc., and all of our operations are conducted through Vera Bradley Designs, Inc. Except where context requires or where otherwise indicated, the terms Company, Vera Bradley, we, our, and us to Vera Bradley Designs, Inc. and its subsidiaries before the Reorganization and to Vera Bradley, Inc. and its subsidiaries, including Vera Bradley Designs, Inc., after the Reorganization. All historical common stock and per share common stock information has been changed to reflect the stock split.

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Our History

Barbara Bradley Baekgaard and Patricia Miller founded the Company in 1982 in Fort Wayne, Indiana, after recognizing a lack of stylish travel accessories in the market. Within weeks, the friends created Vera Bradley, named after Ms. Bradley Baekgaard's mother, and began manufacturing and marketing their distinctive products. The founders, together with the executive management team, have been instrumental in our growth and success. The following timeline sets forth a summary of significant milestones in Vera Bradley's history:

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|------|---|
| 1982 | Barbara Bradley Baekgaard and Patricia Miller launched Vera Bradley by introducing three products: the handbag, the sports bag, and the duffel bag. |
| 1987 | Ernst & Young honored our Co-Founders with an Entrepreneur of the Year award. |
| 1991 | To accommodate the increasing number of attendees, we relocated our annual outlet sale from a tent in our parking lot to its present location at the Allen County War Memorial Coliseum Exposition Center in Fort Wayne, Indiana. |
| 1998 | We founded our primary philanthropy, the Vera Bradley Foundation for Breast Cancer. |
| 1999 | Our products were being sold in all 50 states through Indirect retailers. |
| 2005 | We launched the Vera Bradley Visual Merchandising Program, providing our retailers partners a framework for presenting the brand and merchandising our products in a consistent manner. |
| 2006 | We launched our e-commerce business through our website, verabradley.com. |
| 2007 | We opened a state-of-the-art distribution facility in Roanoke, Indiana. In September, we also opened our first full-price store at the Natick Collection, in greater Boston. |
| 2009 | We opened our first outlet store at Chicago Premium Outlets in Aurora, Illinois. |
| 2010 | We completed our initial public offering. |
| 2011 | We entered the Japanese market, opened the Vera Bradley Design Center in Roanoke, Indiana, and launched our products in 65 Dillard's locations. |
| 2012 | We completed the 200,000 square-foot expansion of the distribution facility in Roanoke, Indiana; increased our presence to all Dillard's locations; and launched a relationship with Von Maur, and are carried in all of their locations. |

The passion for design and customer service established by our founders has driven our growth over the past 30 years and remains the cornerstone of Vera Bradley today. As Chief Creative Officer, Ms. Bradley Baekgaard continues to play a role in the team responsible for our day-to-day creative functions, including product development and store design. Ms. Miller retired in October 2012 as our National Spokesperson, but continues to serve on the Board of Directors.

Evolution of Our Business

Beginning in 2005, we embarked on a series of strategic initiatives designed to take advantage of the growing interest in the Vera Bradley brand. These initiatives were designed to strengthen and enhance our business and operating model, expand our demographic and geographic market opportunity, and position us for future growth. The core components of these initiatives included the following:

Merchandising Strategy. To appeal to a broader range of consumers, we developed a mix of pattern and product offerings specifically targeted at different consumer demographics, refined our product release strategy to

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significantly expand our product portfolio, and increased the number of new patterns released as well as the frequency of new product launches. In addition, we substantially enhanced our visual merchandising strategy, focusing on a consistent presentation of Vera Bradley as a lifestyle brand. In fiscal 2012, we established a dedicated merchant function and elevated the role of marketing to work more collaboratively with the design team to continue improving our process of bringing products to market.

Multi-Channel Distribution Capability. In 2006, we initiated a Direct channel strategy that was designed to expand our brand presence and broaden our consumer demographic while complementing the growing Indirect segment of our business. The first step in establishing the Direct segment of our business was selling directly to consumers through verabradley.com beginning in 2006. In September 2007, we opened our first full-price store. As of February 2, 2013, we operated 65 full-price stores and 11 outlet stores, and 15 department store locations in Japan. In addition, in fiscal 2013 we had more than 61 million visits to verabradley.com.

Infrastructure Investment. Beginning in 2005, we made a series of investments to strengthen our supply chain capabilities, information systems, and product development processes, resulting in substantial cost savings and a more flexible and scalable operating structure. During this period, we shifted our production from a primarily domestic manufacturing model to a more cost-effective global sourcing platform. In 2007, we opened a state-of-the-art distribution facility in Roanoke, Indiana, which was doubled in size to approximately 400,000 square feet as a result of an expansion that was completed in fiscal 2013.

Our Brand

For over 30 years, we have created, developed, and solidified a true lifestyle brand that resonates with a broad range of female consumers. Our brand vision is accessible luxury that inspires a casual, fun, and family-oriented lifestyle. Employees, family members, and friends are often depicted throughout our advertising in fun, friendly, and family-oriented settings, accentuating our brand image in an authentic manner. Our visual merchandising strategy, particularly in our full-price stores, seeks to create the feeling of home. We believe that our lifestyle brand is well positioned to extend into complementary product categories. The strength of our brand is demonstrated during our annual outlet sale in Fort Wayne, Indiana, a sales event that attracts tens of thousands of highly enthusiastic shoppers from across the country.

Our brand positioning emphasizes the high quality, distinctive and vibrant styling, and functional design of our products. At the same time, our frequent releases of new patterns and styles keep the brand fresh, inspire our customers to express their individuality and sense of style in a colorful way, and encourage multiple purchases. We also provide consumers a consistently fresh set of patterns, styles, and products from which to choose that fit with different ages, wardrobes, seasons, and personalities.

We offer a broad assortment of products that meets our customers' different functional needs, including: handbags such as purses, totes, and specialty bags; accessories such as wallets, wristlets, smartphone cases, technology accessories, and eyewear; and travel and leisure items such as weekend bags, duffel bags, and garment bags. We believe this combination of patterns, styles, and products allows us to appeal to all age brackets, including teens, young women, mature women, mothers, and grandmothers. Although our customers represent a broad range of demographic segments, our market research has shown that they generally have a common attitude toward the brand: Vera Bradley is a colorful way of allowing them to express their individuality and sense of style.

Competitive Strengths

We believe the following competitive strengths differentiate us within the marketplace and provide a strong foundation for our future growth:

Strong Brand Identity and Positioning. We believe the Vera Bradley brand is highly recognized for its distinctive and vibrant style. Vera Bradley is positioned in the market as a lifestyle brand that inspires consumers to express their individuality and sense of style. We have also positioned our brand to highlight the high quality and

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functional attributes of our products. The Vera Bradley brand is more price accessible than many competing brands, which allows us to attract a wide range of consumers and inspire repeat purchases.

Exceptional Customer Loyalty. We believe that, as consumers become familiar with the Vera Bradley brand and begin using our products, they become loyal and enthusiastic brand advocates. We believe enthusiasm for our brand inspires repeat purchases and helps us expand our customer base. Our customers often purchase our products as gifts for family members and friends, who, in turn, become loyal customers.

Product Development Expertise. Our product development team combines an understanding of consumer preferences with a knowledge of color, fashion, and style trends to design our products. Our highly creative design associates utilize a disciplined product design process that seeks to maximize the productivity of our product releases and drive consumer demand.

Dynamic Multi-Channel Distribution Model. We offer our products through a diverse choice of shopping options across channels that are intimate, highly shop-able, fun, and characteristic of our brand. Whether they are at a Vera Bradley store, a specialty retail store, a department store, or verabradley.com, we believe consumers have an opportunity to find the brand in places that match their unique shopping interests. Our multi-channel distribution model enables us to maximize brand exposure and customer access to our products.

Established Network of Indirect Retailers. Our Indirect business consists of an established and diverse network of over 3,400 specialty retailers and department store partners. This channel of gift, apparel and accessories, travel, and other specialty retailers, located throughout the United States, provides a strong foundation for our growth. Our Indirect retailers include some of the brand's strongest advocates, and their passion has been instrumental in the development of our brand.

Distinctive Retail Stores. Our stores provide a shopping experience that is uniquely Vera Bradley. We bring the Vera Bradley brand to life in our stores through visual presentation of our wide range of product offerings, the stylish, inviting décor of our stores, and personalized service from our friendly and knowledgeable sales associates. We believe the distinctive shopping experience and personalized service encourage repeat visits and multiple purchases.

Unique Company Culture. We were founded in 1982 by two friends, Barbara Bradley Baekgaard and Patricia Miller, who built our company around their passion for design and commitment to customer service. We believe our founders created a unique company culture that attracts passionate and motivated employees who are excited about our products and our brand. Our employees share our founders' commitment to Vera Bradley customers. We believe that a fun, friendly, and welcoming work environment fosters creativity and collaboration and that, by empowering our employees to become personally involved in product design, testing, and marketing, they become passionate and devoted brand advocates.

Experienced Management Team. Our senior management team led by Michael C. Ray, our Chief Executive Officer, has extensive experience across a diverse range of disciplines in product design, merchandising, marketing, store development, supply chain management, and finance. The current management team has been instrumental in the development and execution of our long-term strategies.

Growth Strategies

We believe there are significant opportunities to expand our business and increase our net revenues and net income through the execution of the following growth strategies:

Grow in Underpenetrated Markets. Our historic growth focused primarily on the eastern United States, and accordingly, the Vera Bradley brand is most recognized in that region. In recent years, we have successfully expanded our Direct and Indirect channels in key developing markets, including in the Midwest and Southwest. In addition, in fiscal 2012 we expanded internationally by entering the Japanese market. We believe the success

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of our expansion efforts is a testament to the strength and portability of our brand and the power of our multi-channel distribution capabilities. We intend to utilize these strengths to further penetrate our existing markets and successfully expand our business into other foreign markets and relatively underpenetrated U.S. markets.

Expand Our U.S. Store Base. We plan to expand our retail presence in the United States by opening new stores. We believe that the market in the United States can support at least 300 Vera Bradley full-price stores. We plan to open approximately 20 new stores annually during each of the next five fiscal years.

Drive Comparable-Store Sales and Our E-Commerce Business. We have several ongoing initiatives to drive comparable-store sales growth, including focusing on store-level merchandising programs and enhancing in-store customer service and selling capabilities. As a key element of our Direct channel strategy, we intend to grow our e-commerce business through focused marketing efforts, online merchandising initiatives, and social networking sites such as Facebook and Twitter. We believe our retail and e-commerce businesses are complementary and facilitate frequent contact with our customers.

Expand Our Product Offerings. We design products to accessorize a woman's life and believe this core competence serves as a platform for growth within and beyond our current product lines. We have expanded our product offerings to include new line extensions, such as focused gift and special occasion offerings, including this year's back to campus and tech accessory products, and brand extensions, such as our paper and stationery collection. We believe that opportunities exist to accessorize a woman's life through complementary product collections that fit within our positioning as a lifestyle brand.

Our Product Release Strategy

We introduce new patterns seasonally. Within each season, we generally introduce two to four patterns. These patterns are incorporated into the designs of a wide range of products, including handbags, accessories, and travel and leisure items, that are part of the core seasonal release. These product assortments each season can be classic styles, updates to older designs, or new product introductions.

Between our seasonal offerings we introduce smaller assortments specific to a category (e.g., a Vera Bradley Baby gift assortment) or customer segment (e.g., a more fashion-forward resort collection).

To keep our assortment current and fresh and to focus our inventory investments on our best performers, we discontinue patterns at regular intervals. We sell our remaining inventory of retired products primarily through our website, outlet stores, and at our annual outlet sale.

Our Products

The following chart presents net revenues generated by each of our three product categories and other revenues as a percentage of our total net revenues for fiscal 2013, 2012, and 2011:

| | Fiscal Year Ended | | |
|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| | February 2, 2013 | January 28, 2012 | January 29, 2011 |
| Handbags | 40.4% | 43.1% | 49.2% |
| Accessories | 31.7% | 32.2% | 31.9% |
| Travel and Leisure Items | 14.7% | 15.2% | 12.7% |
| Other ⁽¹⁾ | 13.2% | 9.5% | 6.2% |
| Total ⁽²⁾ | 100.0% | 100.0% | 100.0% |

(1) Includes primarily home, merchandising, freight, and licensing revenues.

(2) Excludes net revenues generated by our annual outlet sale.

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Handbags. Handbags are a core part of our product offerings and are the primary component of every seasonal assortment. The category consists of classic and new styles developed by our product development team to meet consumer demand and drive repeat purchases. Our handbag product category extends beyond handbags to include totes and specialty bags such as crossbodies, baby bags, backpacks, and laptop portfolios. Handbags play a prominent role in our visual merchandising, and we focus on showcasing the different patterns, colors, and features of each bag.

Accessories. Accessories, our second largest revenue category, include technology accessories and fashion accessories such as wallets, wristlets, eyeglass cases, cosmetics cases, paper and gift products. Our accessories are attractively priced and allow the consumer to include some color in her wardrobe, even if tucked into another bag. Our product development team consistently updates the accessories assortment based on consumer demand and fashion trends.

Travel and Leisure Items. Our travel and leisure product category includes duffel bags, garment bags, rolling luggage, and travel accessories, such as travel cosmetic cases. The first Vera Bradley product offering included duffel bags, which consistently have been a strong performer. We believe their popularity, as well as the appeal of our other travel and leisure items, results from our vibrant designs, functional styles, and lightweight fabrications.

Product Development

We have implemented a fully integrated and cross-functional product development process that aligns design, market research, merchandise management, sales, marketing, and sourcing. Product development is a core capability that makes our products unique and provides us with a competitive advantage. Our designs and aesthetics set our products apart and drive customer loyalty. Our product development team mixes an understanding of the needs of our target customers with knowledge of upcoming color and fashion trends to design new collections as well as new product categories that will resonate in the market.

We typically begin the development stage of our products in the Vera Bradley portfolio 12–18 months in advance of their release. The development of each new pattern includes the design of an overall print, a complementary fabric backing, and three sizes of coordinating trim materials. To seek fresh perspectives, we collaborate with independent designers to create unique patterns for each season. We oversee the development and exercise the final approval of all patterns and designs. Once developed, we generally copyright each pattern, including the print, fabric backing and coordinating trim. We believe that great design is not only central to our product development efforts, but also is a fundamental part of our brand development and growth strategies. In the past several years, we have made investments to evolve and integrate our product development expertise, including opening a design office in New York City, as well as opening a design center in Roanoke, Indiana.

Our product development team works to ensure that new collections contain an assortment of products and styles that are in line with both fashion trends and customer needs and regularly updates classic styles to enhance functionality. In addition, we actively pursue opportunities to expand our product offerings through new line and brand extensions. Our product development team monitors fashion trends and customer needs by attending major trend shows in Europe and the United States, subscribing to trend monitoring services, and engaging in comparison-shopping.

Our product development team is also responsible for assortment planning, pricing, forecasting, promotional development, and product lifecycle management. Forecasting is based on seasonal market research and in-store testing. We gather seasonal market research through a variety of methodologies, including scheduled interviews and online and in-person surveys. We conduct seasonal in-store testing by releasing test products in our full-price stores and evaluating their success in the marketplace prior to product introduction on a larger scale. The team assures that we offer a broad range of patterns, fabrics, styles, and functionality features in a cost-effective manner. We believe that with our cross-functional, collaborative approach, we are able to introduce and sell our merchandise in a way that clearly communicates the Vera Bradley brand and the Vera Bradley lifestyle.

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Marketing

We believe that the growth of our brand and our business is influenced by our ability to introduce and sell our merchandise in a way that clearly conveys the Vera Bradley lifestyle. We use marketing as critical tools in our efforts to promote our brand.

Direct Mail. The seasonal Vera Bradley catalogs are key vehicles for promoting the brand and product portfolio. Each catalog is sent to a targeted customer mailing list. In addition to distributing the catalog, we produce and distribute a number of other marketing pieces, including postcards and mini-mailers. We believe our direct mail media generates excitement and awareness about the brand and seasonal introductions and allow us to reach both new and loyal customers in their homes.

Advertising. We employ print and outdoor advertising to increase overall brand awareness. Our advertisements are placed primarily in national magazines that have a readership similar to our target demographics. These publications have recently included *Seventeen*, *InStyle*, *Better Homes and Gardens*, and *Real Simple*. We continually assess our advertising strategies and tactics.

Public Relations and Product Placement. Vera Bradley has received considerable exposure in the press, including in publications such as *InStyle*, *O the Oprah Magazine*, *Good Housekeeping*, *Southern Living*, and *The New York Times*. In addition, we have expanded our marketing efforts to promote product placement in feature-length films and on prime-time television shows such as *Modern Family* and *New Girl*.

Social Media and Online Marketing. In recent years, we have greatly increased traffic to verabradley.com and have increased awareness of our brand through online marketing and social networking sites. We have captured more than 2.0 million customer e-mail addresses in our online customer file, with many of these customers providing age, occupation, and location data. This captured information provides us with deeper insight into the products and categories that are in the highest demand, and allows us to better target our customers with appropriate messages. As of February 2, 2013, we had approximately 1.4 million Facebook fans, over 52 thousand Twitter followers, and over 3 million visits to our blog, *The Inside Stitch*. We believe these media not only connect us with our fans, but also allow us to target them through cross-channel marketing.

Channels of Distribution

We distribute our products through our Direct and Indirect segments. This multi-channel distribution model not only enables us to have operational flexibility, but also maximizes the methods by which we can access potential customers.

Direct Segment

Full-Price Stores. We have developed a retail presence through our full-price stores, all located in the United States, which provides us with a format to showcase the image and products of Vera Bradley. As of February 2, 2013, we operated 65 full-price stores. Our full-price stores average approximately 1,800 square feet per store. Our stores are designed to create a feeling of home with a high standard of visual merchandising. The welcoming nature of our full-price stores provides our customers with a comfortable shopping experience in a setting that showcases our merchandise and conveys the Vera Bradley lifestyle. Our sales associates are passionate about our products and customer service, which, we believe, translates into a superior shopping experience.

E-Commerce. In 2006, we began selling our products through the verabradley.com website. The objective of verabradley.com is to provide both a mechanism for marketing directly to consumers and a storefront where consumers can find the entire Vera Bradley collection. In fiscal 2013, we invested in upgrades to our website allowing for a more user friendly homepage, enabling us to ship to over 13 international countries, and enhancing the checkout experience. In fiscal 2013, we had over 61 million visits to verabradley.com.

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Outlet Stores. Our outlet stores are a vehicle for selling retired merchandise at discounted prices, while maintaining brand integrity. We believe our outlet stores are an integral part of our distribution strategy, as this format provides an additional channel of distribution for our products and enables us to better target value-oriented customers. Our outlet stores average approximately 3,000 square feet per store. As of February 2, 2013, we operated 11 outlet stores.

International. We launched a marketing campaign to connect with the Japanese consumer on April 18, 2011. This campaign included seven temporary pop-up stores in several department stores including Isetan Shinjuku and Marui Yurakucho located across Tokyo and Kyoto. The international channel includes the Japanese website verabradley.co.jp launched in fiscal 2012. During fiscal 2013, we increased our Japanese presence to a total of 15 department store locations.

Annual Outlet Sale. Our annual outlet sale is held in the Allen County War Memorial Coliseum Exposition Center in Fort Wayne, Indiana. The annual outlet sale is an important tradition for Vera Bradley, has many loyal followers, and is an opportunity for us to sell our retired merchandise at discounted prices in a brand-right fashion. We attracted more than 62,500 attendees to our 2012 annual outlet sale.

Store Location Selection Strategy

Our store location decisions are made case by case, depending on the retail strategy we have developed for the particular market. This includes actual and planned penetration in both Indirect and Direct segments, as well as existing e-commerce demand. At this time, we do not believe any market has been fully penetrated. We believe that expansion of our store base complements our Indirect segment by increasing brand awareness and reinforcing our brand image. In addition to analyzing store economics, we pay particular attention to the location within the shopping center, the size and shape of the space, and desirable co-tenancies. Along with seeking co-tenants that we believe share our target customer, we seek a balanced mix of moderate and high-end retailers to encourage high levels of traffic. Our target full-price store size is approximately 1,800 square feet, but we are able to work with spaces as small as 1,000 square feet or, depending on our market strategy and relevant economic factors, spaces as large as 2,800 square feet.

Store Operations

The focus of our store operations is providing consumers with a comfortable shopping experience. We strive to make the experience interactive through special store events, such as showcasing newly launched products or celebrating our namesake's birthday. Our customer service philosophy emphasizes friendly service, merchandise knowledge, and passion for the brand. Consequently, an essential requirement for the success of our stores is our ability to attract, train, and retain talented, highly motivated district managers, store managers, and sales associates. Our district and store managers are our primary link to the consumer, and we continually invest in their development.

Store Economics

We believe that our innovative retail concept and distinctive retail experience contribute to the success of our stores, most of which generate strong productivity and returns. We expect our full-price stores to average approximately 1,800 square feet per store, and we expect to invest approximately \$0.4 million per new store, consisting of inventory costs, pre-opening costs, and build-out costs, less tenant-improvement allowances. New full-price stores generate on average between \$1.2 million and \$1.4 million in net revenues during the first twelve months, and the payback on our investment is expected to occur in less than 18 months.

Indirect Segment

As of February 2, 2013, we had approximately 3,400 Indirect retailer partners, the majority of which were specialty retailers with whom we have had long-standing relationships. No single account represented more than

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5.0% of total Indirect net revenues in fiscal 2013, with the top ten accounts representing in the aggregate less than 16.0% of total Indirect net revenues. The majority of our Indirect retailers have been customers for over five years. In fiscal 2012, we launched our products in the department store channel.

Sales Force

We believe that having an in-house sales force results in more consistent brand presentation and messaging, enhanced support for our Indirect retailers, and a more predictable, scalable, and cost-efficient business model. As of February 2, 2013, our sales team consisted of 87 in-house, full-time sales consultants. The compensation structure for our sales consultants consists of a combination of fixed pay and sales-based incentives.

In addition to acquiring new and growing existing accounts, our sales consultants serve as a support center for our Indirect retailers by assisting and educating them in areas such as merchandising and visual presentation, marketing of the brand, product selection, and inventory management. Our sales consultants also participate in our semi-annual product introduction and education event for our Indirect retailers. Our visual merchandising program provides our sales consultants with a framework to guide our Indirect retailers regarding optimal product placement and display that is intended to reinforce the message that our brand is distinct from those of our competitors.

Manufacturing and Supply Chain Model

Our manufacturing and supply chain model is designed to maximize flexibility in order to meet shifting demands in the market. Our model utilizes offshore raw material suppliers and a blend of offshore and domestic manufacturing. We place a strong emphasis on continuous improvement and have employed lean manufacturing concepts. Our broad-based, multi-country manufacturing and supply chain model is designed to achieve efficient, timely, and accurate order fulfillment while maintaining appropriate levels of inventory.

Our sourcing strategy is part of the larger cross-functional product development process. The overall objective for our sourcing team is to build and sustain collaborative partnerships throughout our supply chain, with a focus on identifying appropriate countries and partners to manufacture our products. The sourcing team leverages its expertise in negotiation, relationship management, and change management to maintain a strong global supply chain.

We strive to maintain the appropriate balance of inventory to enable us to provide a high level of service to our customers, including prompt and accurate delivery of our products. We have an active sales and operations planning process that helps us balance the supply and demand issues that we encounter in our business, optimize our inventory levels, and anticipate inventory needs. We have also integrated our planning, forecasting, and segmentation processes under one function called Inventory Planning and Deployment. This integrated function along with the creation of a Merchant function, has allowed for further improvements to our inventory management processes.

The majority of our products are cotton-based. Our other products are made primarily from specialty fabrics (including nylon and microfiber) and paper. We source our materials from various suppliers in Asia, with the majority coming from China and South Korea. Our global supply chain and purchasing teams work together with select suppliers enabling us to optimize the mix of cost, lead time, quality, and reliability within our global supply network. All of our suppliers must comply with our quality standards, and we use only a limited number of pre-approved suppliers who have demonstrated a commitment to delivering the highest quality products. In December 2008, we opened an office in Dongguan, China, which enables us to increase our control over the manufacturing and supply chain process and monitor compliance with our quality standards.

A significant majority of our finished goods products are manufactured externally overseas. These products are made by a variety of global manufacturers located primarily in China. We are not dependent upon any single

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manufacturer for our products. When determining the size of orders placed with our manufacturers, we take into account forward-looking demand, lead times for specific products, current inventory levels, and minimum order quantity requirements. Overseas production has resulted in substantial cost savings and a reduction of capital investment. With the oversight of our office in China and our independent contractors, we believe these financial benefits have been realized without sacrificing the level of quality inherent in our products or service to our customers.

The remainder of our products are manufactured in the United States to provide flexibility in our supply chain. This production, almost all of which is internal to Vera Bradley, enables us to manufacture a finished product in two weeks. This capability allows us to manufacture finished product to respond quickly to shifts in marketplace demand and changes in consumer preferences. In fiscal 2013, approximately 7% of our units were produced in our domestic manufacturing facility.

Distribution Center

In 2007, we consolidated our warehousing and shipping functions into one, 217,320 square-foot distribution center, located in Roanoke, Indiana. In fiscal 2013, we completed a 200,000 square-foot expansion of the distribution facility. This highly automated, computerized facility allows Vera Bradley employees to receive information directly from the order-collection center and quickly identify the products and quantities necessary for a particular order. The recent expansion resulted in capacity gains in the areas of inbound receiving, inventory storage, order fulfillment, value-add processing and shipping. The facility's advanced technology enables us to more accurately process and pack orders, as well as track shipments and inventory. We believe that our systems for the processing and shipment of orders from our distribution center have enabled us to improve our overall customer service through enhanced order accuracy and reduced turnaround time.

We strive to maintain the appropriate balance of inventory to enable us to provide a high level of service to our customers, including prompt and accurate delivery of our products. We have an active Inventory Planning and Deployment function that strives to balance the supply and demand issues that we encounter in our business, optimize our inventory levels, and anticipate inventory needs.

Our products are shipped primarily via FedEx and common carriers to our stores, our Indirect retailers, and directly to our customers who purchase through our website. We believe we are positioned well to support the order fulfillment requirements of our growing business, including business generated through our website.

Management Information Systems

We believe that high levels of automation and technology are essential to maintain our competitive position. We maintain computer hardware, systems applications, and networks to enhance and accelerate the design process, to support the sale and distribution of our products to our customers, and to improve the integration and efficiency of our operations. Our management information systems are designed to provide, among other things, comprehensive order processing, production, accounting, and management information for the product development, retail, sales, marketing, manufacturing, distribution, finance, and human resources functions of our business. We use several systems, including MICROS-Retail, SAP, JDA, and SCALE, for our information technology requirements.

Competition

We face strong competition in each of the product lines and markets in which we compete. We believe that all of our products are in similar competitive positions with respect to the number of competitors they face and the level of competition within each product line. Due to the number of different products we offer, it is not practicable for us to quantify the number of competitors we face. Our products compete with other branded products within their product categories and with private label products sold by retailers. In our Indirect business,

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we compete with numerous manufacturers, importers, and distributors of handbags, accessories, and other products for the limited space available for the display of such products to the consumer. Moreover, the general availability of contract manufacturing allows new entrants access to the markets in which we compete, which may increase the number of competitors and adversely affect our competitive position and our business. In our Direct business, we compete against other independent retailers, department stores, catalog retailers, gift retailers, and Internet businesses that engage in the retail sale of similar products.

The market for handbags, in particular, is highly competitive. Our competitors include not only established companies that are expanding their production and marketing of handbags, but also frequent new entrants to the market. We directly compete with wholesalers and direct sellers of branded handbags and accessories, such as Coach, Nine West, Liz Claiborne, Dooney & Bourke, and Michael Kors.

In varying degrees, depending on the product category involved, we compete on the basis of design (aesthetic appeal), quality (construction), function, price point, distribution, and brand positioning. We believe that our primary competitive advantages are consumer recognition of our brand, customer loyalty, product development expertise, and our widespread presence through our multi-channel distribution model. Some of our competitors have achieved significant recognition for their brand names or have substantially greater financial, distribution, marketing, and other resources than we do. Further, we may face new competitors and increased competition from existing competitors as we expand into new markets and increase our presence in existing markets.

Copyrights and Trademarks

The development of each new pattern includes the design of an overall print, a complementary fabric backing, and coordinating trim materials. Once developed, we generally copyright each pattern, including the print, fabric backing, and coordinating trim. We currently have in excess of 500 copyrights.

We also own all of the material trademark rights used in connection with the production, marketing, and distribution of all of our products, both in the United States and in the other countries in which our products are principally sold. Our trademarks include Vera Bradley. We aggressively police our trademarks and copyrights and pursue infringers both domestically and internationally. We also pursue counterfeiters domestically and internationally through leads generated internally, as well as through external sources monitoring use in the market. Our trademarks will remain in existence for as long as we continue to use and renew them on their expiration dates. We have no material patents.

Employees

As of February 2, 2013, we had 2,438 employees. Of the total, 1,319 were engaged in retail selling positions, 361 were engaged in manufacturing functions, 32 were engaged in product design, and 491 were engaged in corporate support and administrative functions. The remaining employees were engaged in other aspects of our business. None of our employees is represented by a union. We believe that our relations with our employees are good, and we have never encountered a significant work stoppage.

Government Regulation

Many of our imported products are subject to existing or potential duties, tariffs, or quotas that may limit the quantity of products that we may import into the United States and other countries or impact the cost of such products. To date, we have not been restricted by quotas in the operation of our business, and customs duties have not comprised a material portion of the total cost of a majority of our products. In addition, we are subject to foreign governmental regulation and trade restrictions, including U.S. retaliation against prohibited foreign practices, with respect to our product sourcing and international sales operations.

We are subject to federal, state, local, and foreign laws and regulations governing environmental matters, including the handling, transportation, and disposal of our products and our non-hazardous and hazardous

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substances and wastes, as well as emissions and discharges into the environment, including discharges to air, surface water, and groundwater. Failure to comply with such laws and regulations could result in costs for corrective action, penalties, or the imposition of other liabilities. Compliance with environmental laws and regulations has not had a material effect upon our earnings or financial position. If we violate any laws or regulations, however, it could have a material adverse effect on our business or financial performance.

Executive Officers

The following table sets forth certain information concerning each of our executive officers:

| Name | Age | Position(s) |
|---------------------------|------------|--|
| Michael C. Ray | 52 | Chief Executive Officer and Director |
| Barbara Bradley Baekgaard | 74 | Co-Founder, Chief Creative Officer, and Director |
| Kevin J. Sierks | 40 | Vice President Controller, Chief Accounting Officer and Interim Chief Financial Officer |
| Kimberly F. Colby | 51 | Executive Vice President Design |
| C. Roddy Mann | 43 | Executive Vice President Strategy & Business Development |
| Matthew C. Wojewuczki | 43 | Executive Vice President Operations |
| Bonita J. Inza | 49 | Executive Vice President Sale & Marketing, Chief Experience Officer |
| David O. Thompson | 48 | Vice President Direct Sales |